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U.S. Policies on Enforcement of Controls

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Executive Secretary

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Staff Study 16
(MDAC Draft of June 7, 1955)
(in consultation with State and Commerce)

CFEP Drafting Group
Economic Defense Policy Review
U.S. Policies on Enforcement of Controls

I. COCOM Enforcement

A. Present Control Arrangements and Understandings

1. Primary controls over the export of strategic goods

It has always been understood in COCOM that the main responsibility for applying and enforcing strategic controls rests with the country from which the shipment originates. In the first two years of COCOM, relatively small attention was given to the manner in which the participating governments implemented the International Lists. Member governments were assumed to have the means of applying and enforcing export controls.

As various ancillary controls and greater emphasis on enforcement have developed, this has been modified to the extent that the cooperation of other countries involved in the transaction as importer, shipper, forwarder, etc. may be enlisted (in accordance with IC/DV, voyage licensing, TAC controls). However, it remains a basic principle that the exporting country must exercise its export controls (normally based on a requirement for individual export license) with due care as to the reliability of the exporter and the final destinee, including end-use checks when necessary. End-use checks are particularly important where the destinee is located in a non-PC with sensitive transshipment areas.

2. Ancillary Controls

a. The IC/DV (import certificate - delivery verification) system was the first of the ancillary controls, adopted early in 1951 with the

objective of deterring diversions otherwise enabled by transshipment facilities and assisting export control authorities in determining the legitimacy of an export application. IC/DV has become an important adjunct of primary export licensing procedures exercised by COCOM PC's and to a limited extent by several non-COCOM countries.

Operating problems and proposals for improving the effectiveness of the system have been discussed periodically among COCOM countries. The most notable improvement has been the government-to-government transmittal of copies of IC's. This together with other improvements appear to have substantially eliminated forgery at least of IC's and other fraudulent devices used by illicit traders.

b. The TAC (transit authorization certificate) system was put into effect in January 1955 by the COCOM countries, and was the main new enforcement feature of the 1954 revision of COCOM controls, providing a basis previously lacking for preventing transshipments of embargo items to the Soviet bloc. The TAC scheme has not been in operation long enough to permit a real testing and evaluation, but it seems clear that several of the PC's have taken a narrower view of the TAC system than had been anticipated by the US and others, reducing its effectiveness as a means of stopping diversions as well as raising questions as to the proper operation of TAC and complicating considerably present efforts to extend the TAC system to non-COCOM countries. (as source countries)

c. Transactions controls are in effect in the US, UK and Canada. Other COCOM countries have indicated that their existing financial controls

would accomplish the intent of transactions controls in controlling offshore transactions between their residents and Soviet bloc countries in goods of strategic significance. The Dutch have long claimed that they made no distinction between strategic goods exported from the Netherlands and those commodities which were purchased abroad and sold by a Netherland's firm to a third country. In discussions prior to the 1954 revision they refused to adopt transshipment controls (i.e. TAC) until the UK would agree to exercise transactions controls. The British agreed to adopt transactions controls as a result of the 1954 list reduction.

While there are questions under study in the Executive Branch as to the adequacy of UK transactions controls, there has not been sufficient experience with them to identify positively any major problems. Other questions as to interpretation of transactions control regulations have arisen in the context of stoppages under TAC.

d. Voyage Licensing and Bunkering Controls. Viewed in the context of the comprehensive system of special China controls, voyage licensing and bunkering controls have been of considerable value in restricting the flow of strategic goods to Communist China and North Korea from countries not cooperating in the UN embargo by preventing the carriage of embargoed goods to such destinations in flag vessels of PC's and denying bunkering to any vessels carrying embargoed goods.

Many of the shortcomings in the voyage licensing system have been eliminated. However, its effectiveness would be increased were it to be applied to any shipment known to be destined to Communist China whether or not they were actually delivered there by the vessel in question. Its

effectiveness would also be increased were it to apply to voyages to all Far East Communist ports (and not only Communist China and North Korea) in view of the possibility of subsequent transshipment. The UK has considered such extensions of the system to be unwarranted in the absence of conclusive evidence as to these shortcomings. Thus far the U.S. has not been in a position to bring forward such evidence as would be necessary for the negotiation of tightened controls.

3. Multilateral Exchange of Information on Illegal East-West Trade Transactions.

In June 1954 COCOM worked out a procedure for multilateral consideration of diversion cases (COCOM Doc 1634). This provides for: - coordination by interested COCOM delegates of live cases in order to prevent the diversion of strategic shipments and ~~also~~ for discussion of closed cases to illustrate loopholes in enforcement techniques. It was the US intent that this procedure would serve to develop greater awareness in other COCOM countries of the need for stricter enforcement and would also stimulate direct representations by them to countries responsible or involved in diversion cases rather than relying on US representatives as intermediaries.

To date relatively few discussions of cases have been initiated in COCOM under these procedures. There have been various reasons, including apathy or reluctance on the part of various PC's and some limitations on initiation of cases by the U.S. Means to bring about increased discussion of enforcement cases in COCOM are under consideration in the EDAC agencies, including a proposal for meetings of technical investigative and enforcement officials of the PC's under COCOM auspices.

4. Extension of COCOM Agreements and Understandings to Non-COCOM Countries.

In the enforcement field this is likely to remain a significant and time consuming exercise. Those third countries which have an export trade in strategic items have for the most part indicated their intention to cooperate with the purpose of the International Lists or Battle Act List in not allowing direct exports of embargo items to the bloc. However, it is in connection with better application of source controls and adoption of TAC and IC/DV, so as to prevent indirect shipments to the bloc, that greater success is needed.

The cooperation of a number of non-COCOM countries appears to be especially important to the success of the TAC scheme. The US, with help from the UK and France, have conducted most of the third country approaches on behalf of COCOM. A few non-COCOM countries have already agreed to cooperate in TAC.

IC/DV procedures have already been adopted in whole or in part by Austria, Switzerland (blue certificate), Yugoslavia, Peru, Mexico (Cobre de Mexico), Chile (some copper exports).

The problem countries comprise those which are significant as transit points in Europe and the Mediterranean area and a few which have a significant export trade in strategic items, such as Chile and Mexico. Certain of these have posed delicate negotiating problems, however, made more complex by the fact that the Netherlands and possibly other COCOM transit countries appear to expect fairly complete export control systems on the part of the

third countries and public identification with the TAC scheme before they can be recognized as participants in TAC.

II. U.S. Enforcement Measures Taken on a Bilateral and/or Unilateral Basis

A. US Measures

1. Battle Act Termination of Aid Provisions (Title I and Title II)

On seven occasions, the President has announced his decision to continue aid to specific countries when there had been shipments of items specified under Category B Title I of the Battle Act, on the basis that it would be contrary to US security interests to terminate aid. These shipments have amounted to _____. There has been no instance of termination of aid under the Battle Act. Most of the COCOM countries have been the subject of Battle Act exceptions, as well as Austria, Israel, and Iran. ~~Most of~~ the cases arose from prior commitments, and were discussed in COCOM prior to inclusion in trade agreements.

COCOM procedures for prior consultation and exceptions have served to deter the inclusion of embargo items in new trade commitments, ~~and in~~ bilateral discussions pursuant to Battle Act termination of aid provisions have also worked toward this end. In addition, there have been reports from certain non-COCOM countries that improvements were instituted in the application of local controls following discussions with local officials of cases which, had they not arisen from administrative error, would have been the subject of Battle Act determinations.

2. Administrative Action Program

This program (which is one of withholding certain US privileges from foreign firms which are reported to have participated in diversions) in the past year has had some revisions designed to encourage the other partici-

pating countries to assume their responsibilities in enforcing strategic trade controls. Solo efforts by the US to police international controls may have tended to expend goodwill unnecessarily and to "wear out our welcome". These revisions have also been intended to make the program more adaptable to the circumstances which generally prevail in individual cases and more acceptable to foreign governments.

3. Compliance Proceedings - Department of Commerce

While criminal penalties are provided in the Export Control Act of 1949, it is seldom that evidence can be obtained in a form that is required under US criminal law for the conviction of either a US or foreign national. Thus, increasing emphasis has been placed on the employment of administrative sanctions against both US and foreign violators, using the compliance proceeding.

Unlike the black list techniques of World War II, compliance proceedings have served to give foreign countries and their nationals an assurance that the US would give them the same fair notice and hearing, the same kind of due process, that it would extend to US nationals.

The sanction itself is imposed by a published order issued by the Department of Commerce. Since the beginning of the cold war about 200 cases have been instituted, of which about one-third have been against foreign nationals. (The total of US and foreign nationals suspended is well over 500.)

The decision of whether or not to institute a case against a foreign national involves consideration not only of the offense itself but also such factors as the impact of the case on the country of the violator and the deterrent effects that the case may be expected to have on other traders and possibly even other countries.

4. Foreign Assets Control

5. Controls Over Foreign Sales of Surplus Strategic Equipment

Consideration of the problem of working out control measures to prevent the diversion to the Soviet bloc of strategic items sold locally from US overseas surplus was undertaken some time ago when it came to light that strategic goods from surplus stocks, in particular automotive parts, were moving by indirect means to the Soviet bloc following normal overseas surplus disposal sales. Recommendations for safeguards which should bring about adequate controls were devised by representatives of USRO/ST, CINCEUR, USAFE, USAREUR, and USFA and are under review in Washington. A member of the USRO/ST staff returned to Washington early in June to participate in an inter-service conference called by the Department of the Army on overseas surplus property disposal.

6. Diversion Control Net and Related Activities, Including Intelligence Collection

Arrangements for preventing diversions of strategic shipments to the Soviet bloc have constituted a major part of the enforcement program. In Washington this led to the development of the Diversion Control Network (DCN), an inter-agency group chaired by MDAC with the Departments of State (ECD), Commerce (BFC), Treasury (FAC), Defense (OSD), and CIA all represented. In the field, Economic Defense Officers were designated in all the principal posts, and a European regional coordinator designated in USRO/ST.

The DCN has served to improve the coordination and pooling of efforts and to ensure that in any particular case each agency knows who has action responsibility. It has also been concerned with evaluating the effectiveness of controls, uncovering weak spots and developing improved

enforcement techniques, backstopping and instructing US missions and the delegation to COCOM in specific diversion control activities. 25X1C

The importance and magnitude of the diversion control problem was illustrated recently by a [redacted] study on shipments of copper from the Free World to the Soviet bloc in 1954. The study concluded that about 80,000 tons of embargoed forms of copper reached the bloc despite COCOM controls.

The DCN is heavily dependent upon intelligence support and an effort is now being made to increase [redacted] support for DCN and other enforcement activities. 25X1C

7. Watch List and Other Commercial Intelligence Operations.

All of the US agencies which administer export controls maintain and exchange information about US and foreign individuals and firms suspected or known to be engaged in illicit East-West trade and other kinds of violations of export control regulations. These are confidential lists and are mainly used in the screening of applications for export licenses. The BFC Special Check List is often called the "Watch List" by those officials who work with it. It also serves to alert Foreign Service and other Government officials to particular firms or individuals whose activities might require more than routine attention, end-use inquiries, etc.

There has never been acceptance in COCOM of an international watch list of suspect firms or individuals, except for identifying Communist controlled firms in Austria.

8. Exchange of Technical Teams

There have been visits to the US of technical teams from all but three of the COCOM countries, while teams of US experts have now visited seven of the most prominent COCOM countries. These have served to bring about better knowledge and mutual understanding of each other's control policies, licensing procedures, enforcement techniques, and inspection methods. There have also been occasional informal discussions of policy questions in connection with these visits.

Just as greater initiative in enforcement activities by other PC's is desired, it has long been felt that the most desirable future development in exchanges on technical teams would be exchanges between the European PC's themselves. The most promising field for this appears to be in implementing and improving the TAC scheme.

Analysis of Problems and Deficiencies of Encorcement

The problems and deficiencies in the enforcement program may be placed into two categories -- one relating to the multilateral aspects, the other to the unilateral or bilateral phases. Strictly speaking, it is difficult to separate the two since activities in which we engage unilaterally cannot fail to have some effect on our multilateral relationships.

On the international side the development of the enforcement program has been achieved only with considerable negotiating delays and difficulties. Agreement on TAC and UK transactions controls were part of a quid pro quo for the August 1954 list reduction. Five months of additional negotiations were required before these controls actually were implemented.

The lack of enthusiasm for the enforcement program is based on a number of factors. Possibly the most important of these is the current

political climate prevailing in Europe ~~at this time~~ which influences the attitudes of PC governments toward the entire control program. As the hope for coexistence grows, it can be expected that enthusiasm for the program will diminish.

More specifically there are the following:

a) Reluctance of some countries to adopt enforcement measures unless all interested countries adopt similar measures;

b) Emphasis of foreign government economic agencies on trade promotion rather than trade control;

c) Confidential nature of controls in some countries;

d) Understaffing of enforcement agencies; insufficient orientation of enforcement personnel re the objectives of the program;

e) Reluctance of foreign enforcement personnel to discuss mutual problems with US Embassy officers;

f) Poor or unreliable intelligence information; inability to investigate unevaluated intelligence information.

Additional problems arise from the non-uniformity of controls between PC's and from inadequate legal bases for such controls. Without adequate legal bases not only is it impossible to exercise satisfactory licensing controls, including the use of end-use checks and other precautionary measures, but it is also difficult to impose strong enough punitive action to deter violations of controls. A corollary problem is the frustration of the officials responsible for the implementation of controls caused by personnel shortages and other factors.

Perhaps the most active and troublesome problem in the enforcement area is that caused by the differential level of controls over trade with the Soviet bloc in Europe and Communist China. At the time of the 1954 List reduction the PC's agreed that the List changes would not be applicable to trade with China, that exports to the Soviet bloc (Europe) should not frustrate those covering trade with China, and exports to the Soviet bloc in Europe should not be approved if it was likely that they would be diverted to China. There has been little evidence of denial of exports under these circumstances. In fact, the quantity and value of known diversions to China via the European Soviet bloc Europe and Western countries have been significant. Diversions on non-I/L I goods to China have been facilitated by the removal from licensing, except to China, of most I/L III and China Special List items and by the applicability of IC/DV to only Munitions, AE, I/L I, and II items and of TAC to only Munitions, AE, and I/L I items.

Of the problems referred to above only the last (relating to the differential level of controls) is a serious one. However, with the general resistance by the PC's to any extension of controls, albeit small, plus the desire on the part of most PC's to reduce the level of China controls to the COCOM level, it is most doubtful if we can obtain any tightening of enforcement measures applicable to China trade. Our future course of action in this area is dependent on the outcome of the over-all review of security trade control policy, in particular that covering trade with China.

For the other problems we can only point out to the PC's deficiencies as they occur and press for the small modifications required to effect improvements. To this end the exchanges of teams of technical experts initiated by the US can go far to impress upon the PC's the importance which we attach

to effective enforcement and provide an orientation for foreign governments of US policies, standards, and procedures.

The US has also experienced certain problems originating in its unilateral enforcement activities. From the beginning the US has found itself in the position of international policeman in the enforcement of trade controls, particularly in cases involving non-US goods. We have passed on to foreign governments intelligence information relating to diversions of non-US origin goods, have conducted our own investigations, have pressed for foreign investigations and appropriate action, have coordinated action by several PC's, and have taken administrative action against foreign firms involved in illegal trade. Our activities have been received by the PC's with mixed feelings. It is doubtful whether our interest is ever appreciated by the PC's, but usually it is accepted at least passively because of the Battle Act implications. Our ability to act in the enforcement area varies from country to country, to the extreme that in certain countries we are restricted to contacts with the Foreign Offices and may be politely told that investigations involving non-US origin goods or nationals should not be of concern to us. Our taking of administrative action is usually resented, at best only tolerated. This attitude on the part of foreign governments is especially pronounced when their firms have actually not violated local laws or regulations and they accordingly consider US interest and action as unjustified interference. Because of this feeling the US modified its Administrative Action program last year to change its basis from one of prejudging liability under foreign law and to encourage investigations of AAP cases by foreign governments.

The extent to which U.S. goodwill is expended in pressure for enforcement can be evaluated partly in terms as to whether the goods in question are U.S. or non-US origin. Also it should be emphasized that it is not a mere expenditure of goodwill that should concern us as much as the question of whether the expenditure is made wisely or wastefully.

With respect to illicit East-West trade in non-US origin goods, the most serious U.S. problems come from friendly countries' embarrassment when we expose inadequacies in particular cases or in the general aspects of their programs. Much of this, of course, hinges on how we make our approaches. If we give to the countries concerned the information that we obtain about diversions so that they can take actions themselves, we will naturally cause less embarrassment than if we publicize to others their weaknesses. Essentially our problem for the future would seem to be to find the most diplomatic ways of bringing pressure so as to persuade friendly governments themselves to improve their controls and to take action against violators.

In the case of U.S. origin goods, some countries have taken the position that U.S. strategic materials which are processed or made components of products of more or less different nature are "nationalized" (i.e. origin changed) by those actions; accordingly the U.S. should have no right to object to shipments to the bloc of the finished product. This brings up, of course, the whole problem of PD 810 policies. In addition, some countries object to investigations conducted by U.S. Foreign Service personnel of the activities of foreign nationals engaged in illegal diversions of U.S. goods on the grounds that such investigative activities constitute an invasion of

sovereignty or even commercial espionage. Certain countries have objected to our imposition of sanctions against participants having only a marginal role in diversions -- e.g., freight forwarders, carriers, banks, etc. However, since the beginning of security controls we have had only one cause celebre involving complaints by a foreign country against the U.S. for imposition of compliance action against one of its nationals. Under these circumstances claims of embarrassment and fruitless expenditure of goodwill may not be too well founded.

On the question of enforcement of U.S. controls over non-IL commodities we must bear in mind our long time premise that COCOM controls are only the minimum which any PC is permitted to impose over its commodities. Further, it has been agreed in COCOM that source countries have primary responsibility for the control of their own goods. Our problems vary depending on whether the goods are Positive List items or under only General license control. Our determination that goods are sufficiently strategic to warrant unilateral control regardless of COCOM agreement should be made with the realization and desire to undertake whatever action is necessary to enforce these controls. Goods under GRO control (i.e., non-strategic or non-short supply) do not provide similar justification for full enforcement control and the needless expenditure of goodwill. However, we cannot ignore them completely since domestic considerations such as political and public relations enter into even this field. Obviously, from the U.S. point of view, the problems in trying to use U.S. export control enforcement in the general license commodity field are quite substantial; the present U.S. control system as applied to such commodities represents a number of administrative and public relations

compromises that have the ultimate effect of making our enforcement in this area considerably weaker than in the area of Positive List commodities.

Possible Future Courses of Action

It would be desirable if the problems and deficiencies in the enforcement field as described above could be corrected. However, without some drastic change in the over-all control policy it is unlikely that more than routine procedural modifications can be effected in existing controls. Such measures as the TAC scheme, transactions controls and voyage licensing are not completely adequate in complementing the entire range of primary controls. We have been unsuccessful in past efforts to extend these controls to cover a wider range of items, i.e., I/L II, III and the China Special List or to have them apply to the China trade area. Without/a further downward revision in the lists or a basic change in the differential levels of control in trade with China, few PC's will be willing to adopt more rigid enforcement measures. If we were to embark on an extensive program of negotiations with other PC's we would only antagonize them and dissipate the negotiating goodwill required for more important problems not only in the economic defense field but also in the broader area of East-West policy.

If we assume that the need for control of exports will continue for the indefinite future and that during this time there is little likelihood of obtaining any substantially tighter and broader international control, the question arises as to what we should do about US export controls. At the present time US export control enforcement is admittedly not the most effective that could be devised; this condition of course has obtained since the commencement of the cold war. The enforcement program has repre-

sented a number of compromises which have taken into account business and administrative limitations and the lack of appropriately trained personnel to conduct investigative operations abroad, the spot checking on a percentage basis of shipments by customs, etc. The licensing processes and the size and position of the enforcement organization are illustrative of what might be called a realistic evaluation of the relative importance of enforcement in the over-all program. Consequently when we think of the future we should not only think of a possible continuation of the present level and kind of enforcement versus a dilution to the lowest common denominator of international controls, but also give some thought to possibilities of unilateral tightening of US controls, if it appears that need exists for such. We must always remember that our control system and enforcement program with all its limitations is at a substantially higher level than the comparable programs of cooperating countries.

Realizing then that our enforcement program could be tightened, with justification in the List reduction and CG agreement for improved enforcement, let us consider some ways in which this tightening could be accomplished. For one thing we could consider using additional especially trained personnel abroad to supplement the present activities of FSO's in this field; recognizing the inadequacies of the TAC scheme to cope with diversions, we could if such action is warranted, as the British did in World War II, institute a system whereby we would permit US strategic goods to move only to freight forwarders who would sign written undertakings not to accept or carry out instructions to divert to the bloc. Since the forwarders are key institutions in the transit countries this would have a substantial preventive effect. In

addition we could require the destination control notice on all bills of lading and commercial invoices.

The advantages of tighter enforcement procedures would be increased security with less risk of diversion and possibly greater Congressional approval for the implementation of the export control program. On the other side, however, would be the additional foreign criticism which would result, slow up in movement of exports (with probable complaints from the US export trade), and increased costs of operating the extra controls. These latter arguments could be used with equal effect in support of lower standards of enforcement. In favor of maintaining the present level of enforcement we may state that our current policies and procedures are already known to and accepted by foreign governments as well as Congressional, trade, and other public groups; further they are reasonably efficient at an easily assessed cost which is not out of line with other control operations. On balance, and in the light of the conclusions outlined above for the international program, it probably would be preferable to maintain the status quo in U.S. enforcement policy (except for obvious changes which can be made to plug loopholes) pending some major change in our over-all economic defense policy.

A second course of action is to continue our efforts to enlist non-PC cooperation and participation in enforcement measures. The most immediate problems in this regard are our pending negotiations with certain Latin American, European, and Near Eastern countries for the institution of the TAC scheme and IC/DV system. Additional study can also be given to the inadequacies in the basic control systems of these and other non-PC's.

The general consensus of the EDAC agencies is that there is an open field for improvement of:

1) intelligence collection and dissemination;

2) better collaboration between US element abroad which would assist in the more satisfactory implementation of already existing enforcement measures.

It is generally not considered an appropriate function of the Foreign Service to engage in the covert collection of information on illegal East-West trade and for this reason is neither staffed nor organized to do so. An expanded effort on the part of the intelligence collection agencies in the field of East-West trade would undoubtedly bring forth an increased volume of information.

Another important course of action is to encourage cooperation and multilateral exchanges of information in the handling of illegal East-West trade transactions. Specifically we should press other PC's to employ the COCOM procedures outlined in Doc. _____ and to support the activities of the COCOM Sub-Committee on Export Controls. An additional proposal would be for the establishment of a COCOM Sub-Committee for the interchange among the technical investigative and enforcement experts of the PC's of useful investigative and related information. Such a Sub-Committee would provide a basis for understanding and cooperation among the investigative and enforcement staffs of the various PC's not obtainable through the existing Sub-Committee structure. Our efforts toward these ends should be with a view to encouraging more active participation by other PC's and toward a de-emphasis of U.S. initiative and bilateral pressure. To the extent that other countries

adequately assume their full responsibilities in the program, the U.S. can withdraw from its unpopular position abroad as policeman and agitator for increased controls.